Irving Trust

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Economic Research & Planning Division

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Record rates were set in the Treasury refunding auctions this week, reflecting dealer apprehensions concerning the strength of investor interest, as well as the unsettled nature of the funds market. Depending on one's point of view, the auctions were either very successful or only moderately so. The stronger than expected investor interest--and the consequently slightly lower than expected yields--were a relief to securities dealers, who feared being burdened with heavy inventory positions in the new notes and bonds. The Treasury cannot have been similarly enthusiastic, however, in view of the record high rates placed on the offerings. Nevertheless, with the refunding out of the way, the market's tone should improve somewhat before the Labor Day doldrums set in.

As anticipated last week, the funds market was highly volatile after the weekend. The main reason appears to have been the unpredictability of the impact of the air traffic controllers' strike on Federal Reserve float. As noted here last week, the best guess was that delays in check transit via the Fed's chartered air couriers would cause float to increase substantially, oversupplying the banks with reserves. In fact, the almost optimal visual flying conditions throughout the country appear to have minimized the impact. That could change quickly, of course, if weather conditions worsen. But during the last week, float probably provided less reserves than expected by the Fed, accounting for much of the upward pressure on the funds rate. The Fed, for its part, appeared to be trying to catch up with the problem with repeated reserves injections, but nevertheless the rate moved up sharply, from about 17 1/2% at the Monday opening to over 20% at some points.

Open market operations in coming weeks are highly uncertain. Both a sudden increase in float and settlement of the Iranian transfer could necessitate reserves draining operations or else smaller additions. That is hardly a propitious background for a market rally, though on balance judgment suggests that the funds rate should move back down under 18% soon.

The Federal Open Market Committee meets next on August 18, against a background of recently sluggish economic activity. M-1B (adjusted for estimated shifts of NOW accounts) is well below the bottom of its target range, while M-2 growth appears rapid. Most of the strength in M-2, however, is attributable to rapid growth of money market mutual fund shares, which last week surpassed $140 billion. Our best guess is that at its meeting the FOMC will vote for another modest move to make reserves more available to the banking system. That in turn will put some downward pressure on interest rates.

William C. Melton

Note: The full text of this letter is available to Telerate subscribers on pages 7250-51 on the Monday morning following the Friday date of the letter.

	8/7/81 (Noon)	Week Ago	Year Ago
Prime Lending Rate at Irving Trust Company	20.50%	20.50	11.00%
Effective since	7/8/81		
Discount Rate at Federal Reserve Bank	14.00	14.00	10.00
Federal Funds	18.75	17.38	9.13
Repurchase Agreements	18.50	16.25	8.88
U.S. Treasury Issues			
Bills			
3 months	16.29	15.50	8.70
6 months	16.96	16.13	9.13
1 year	16.66	16.00	9.30
Coupons			
2 years	16.00	15.75	9.65
4 years	15.65	15.38	9.98
7 years	15.05	14.88	10.50
10 years	14.84	14.63	10.75
Long Bond	14.10	13.88	10.65
Negotiable Certificates of Deposit-Secondary Market			
1 month	18.25	17.70	9.15
3 months	18.20	17.70	9.30
6 months	18.05	17.70	9.50
1 year	17.20	16.85	10.00
Banker's Acceptances			
1 month	18.25	17.60	9.15
3 months	18.25	17.75	9.25
6 months	18.15	17.90	9.55
Eurodollar Deposits			
1 month	19.00	18.50	9.63
2 months	19.00	18.63	9.88
3 months	19.00	18.63	10.19
Commercial Paper - Prime Names			
Directly placed by:			
Finance Companies			
1 week	18.25	17.25	7.00
1 month	17.75	17.38	8.63
3 months	16.50	16.50	8.75
Bank Holding Companies			
1 month	17.75	17.13	8.63
Dealer Placed:			
3 months	18.00	17.13	8.63
New AA Corporate Utility Bond	17.00	17.13	12.50
Tax Exempt			
6 month Project Notes	7.85	7.80	4.35
1 year AAA Bond	8.40	8.00	5.00
5 year AAA Bond	9.00	9.00	5.40
20 year AAA Bond	10.25	10.50	7.95

This information represents prevailing market yields.
It should not be construed as an offering.
All yields are on the offered side of the market.

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